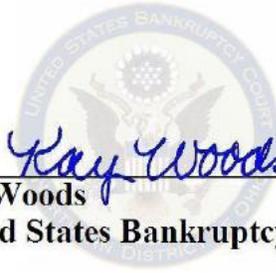


IT IS SO ORDERED.

Dated: May 7, 2012
04:58:26 PM


Kay Woods

Kay Woods
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO

IN RE:

CARL V. MACE and
CINDY A. MACE,

Debtors.

* * * * *

THOMAS R. SKELTON and
AMY L. SKELTON,

Plaintiffs,

v.

CARL V. MACE and
CINDY A. MACE,

Defendants.

CASE NUMBER 10-42899

ADVERSARY NUMBER 10-4239

HONORABLE KAY WOODS

TRIAL OPINION REGARDING COMPLAINT
TO DETERMINE DISCHARGEABILITY OF DEBT

This adversary proceeding is a classic example of the Clare
Boothe Luce adage, "No good deed goes unpunished." The evidence in

this case establishes that the Plaintiffs performed the good deed of guaranteeing a corporate debt and putting up their farm as collateral for such debt without ever receiving anything of value in return.

Plaintiffs Thomas R. Skelton ("Skelton") and Amy L. Skelton a/k/a Amy Montgomery (collectively, "Plaintiffs") filed a proof of claim denominated Claim No. 18-2 in the amount of \$313,781.36 based on "breach of contract, conversion, indemnification, contribution, subrogation, fraud, and misrepresentation" ("Debt") (Claim No. 18-2 at 1) arising out of the transactions that are the subject of this adversary proceeding. The Plaintiffs filed Complaint (Doc. # 1) initiating this action on November 1, 2010, seeking the Court to find that the Debt is non-dischargeable pursuant to 11 U.S.C. § 523(a)(2), (a)(4) and (a)(6). On December 10, 2010, the Debtors/Defendants Carl V. Mace ("Mace") and Cindy A. Mace (collectively, "Defendants") filed Answer (Doc. # 6).

The Court conducted a trial on February 29, 2012 ("Trial"), at which appeared (i) John H. Chaney III, Esq. on behalf of the Plaintiffs; and (ii) Gary J. Rosati, Esq. on behalf of the Defendants. Following the Trial, the Court took this matter under advisement. For the reasons set forth herein, the Court will enter judgment in favor of the Defendants.

This Court has jurisdiction pursuant to 28 U.S.C. § 1334 and the general order of reference (General Order No. 2012-7) entered in this district pursuant to 28 U.S.C. § 157(a). Venue in this

Court is proper pursuant to 28 U.S.C. §§ 1391(b), 1408 and 1409. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(I). The following constitutes the Court's findings of fact and conclusions of law pursuant to Federal Rule of Bankruptcy Procedure 7052.

I. BACKGROUND

A. Complaint

The Complaint asserts that the Defendants are liable to the Plaintiffs in an amount in excess of \$350,000.00.¹ The Plaintiffs request the Court to enter judgment against the Defendants for the Debt or, in the alternative, to abstain from entering judgment in order to permit the Court of Common Pleas for Mahoning County, Ohio ("Mahoning Court") to render judgment. The Plaintiffs' Complaint alleges that the Debt is non-dischargeable pursuant to § 523(a)(2), (a)(4) and (a)(6).

B. Bankruptcy Case

The Defendants filed a voluntary petition pursuant to chapter 13 of the Bankruptcy Code on July 30, 2010, which was denominated Case No. 10-42899 ("Main Case"). On September 27, 2010, the Defendants filed Amended Chapter 13 Plan ("Plan") (Main Case, Doc. # 26). The Plan has not been confirmed by the Court because certain claims needed to be resolved in order to determine feasibility of the Plan. On November 4, 2010, the Plaintiffs filed Claim No. 18-1, which asserted an unsecured claim in the amount of

¹This was the amount of Claim No. 18-1. Amended Claim No. 18-2 reduced the Debt to \$313,781.36.

\$350,000.00 for “[f]raud and [m]isrepresentation.” (Claim No. 18-1 at 1.) On March 29, 2011, the Plaintiffs filed amended Claim No. 18-2 for the Debt. The Defendants filed Amended Objection to Proof of Claim # 18-2 (“Objection to Claim No. 18-2”) (Main Case, Doc. # 113) on May 26, 2011, which sought to disallow Claim No. 18-2. On July 28, 2011, the Plaintiffs filed Motion for Leave to File Amended Claim (“Motion for Leave”) (Main Case, Doc. # 128), which requested leave, *nunc pro tunc*, to March 29, 2011, to file Claim No. 18-2.

On July 28, 2011, the Court held a hearing on the Objection to Claim No. 18-2 and the Motion for Leave, at which Mr. Chaney and Mr. Rosati appeared. Following the hearing, on that same date, the Court entered (i) Order Overruling Objection to Claim 18-2 (Main Case, Doc. # 130); and (ii) Order Granting Motion for Leave (Main Case, Doc. # 131). In the Order Granting Motion for Leave, the Court concluded, “Claim No. 18-2 is deemed timely filed.”² (Order Granting Mot. for Leave at 1.)

C. Stipulation of Facts

On February 28, 2012, the parties jointly filed Stipulation of

²On March 11, 2011, the Defendants filed Motion to Dismiss (Doc. # 9), which requested the Court to dismiss this adversary proceeding on the basis that Claim No. 18-1 had been disallowed. On August 2, 2011, the Court entered Order Denying Motion to Dismiss (Doc. # 16), in which the Court stated,

Based on the subsequent filing of Claim 18-2 and the Court’s ruling that Claim 18-2 is timely filed, the basis for the Motion to Dismiss – *i.e.*, the Plaintiffs do not have a claim pending against the Defendants – is no longer accurate or applicable to the instant adversary proceeding. . . . As a consequence, the Court hereby denies the Motion to Dismiss.

(Order Denying Mot. to Dismiss at 8.)

Facts ("Stipulation") (Doc. # 35), which was admitted into evidence at the Trial. The Court hereby incorporates by reference all of the facts set forth in the Stipulation.

II. TRIAL

The parties waived opening statements. The Plaintiffs presented the testimony of (i) Mace on direct examination; and (ii) Skelton on direct examination and re-direct. Mace and Skelton were cross-examined by Mr. Rosati on behalf of the Defendants.³ The Defendants presented the testimony of Mace on direct examination and re-direct. Mace was cross-examined by Mr. Chaney on behalf of the Plaintiffs. The facts set forth herein are based on the Stipulation and the testimony of Mace and Skelton.

Following the Plaintiffs' case-in-chief, the Court admitted into evidence Exhibits A through G, I and K.⁴ Following the Defendants' presentation of evidence, the Court admitted into evidence Exhibits 1 through 15 and 20.⁵ Neither party objected to the authenticity or admissibility of any exhibit. Each party made closing arguments.

³At the conclusion of the Plaintiffs' case-in-chief, the Defendants orally moved for a directed verdict. At that time, the Court found that questions of fact remained and, thus, denied the motion for a directed verdict.

⁴The Plaintiffs' exhibits are labeled "Plaintiff's [sic] Exhibit A" through "Plaintiff's [sic] Exhibit K." The Court will refer to these exhibits as "Exhibit A" through "Exhibit K."

⁵The Defendants' exhibits are labeled "Exhibit Defendants 1" through "Exhibit Defendants 20." The Court will refer to these exhibits as "Exhibit 1" through "Exhibit 20."

A. Mace Testimony

Mace testified that he and Timothy Kelly ("Kelly") formed K&M Feeds, Inc. ("K&M") in 1995 to sell livestock feed, hardware, animal supplies and farm supplies. At that time, Mace and Kelly each received 1,000 shares of K&M stock. K&M operated its business at 1994 Mercer-New Wilmington Road, New Wilmington, Pennsylvania ("K&M Store"), which was adjacent to real estate upon which Skelton owned and operated a livestock auction. Mace stated that, as president of K&M, he controlled the daily operations of K&M from its formation in 1995 through 1997. During this time, Kelly was employed by K&M and served as its secretary and treasurer. Beginning in 1998, Kelly took control of K&M, although Mace remained its president. Kelly remained in control of K&M's daily operations until January 1, 2002, when Kelly transferred his 1,000 shares of K&M to Mace. From January 1, 2002, through cessation of the business in 2009, Mace was the sole owner of K&M, during which time he made all business decisions for the company.

Mace stated that, on January 1, 2002, he and Kelly entered into the One-Year Agreement,⁶ whereby Mace became the sole owner of K&M. In exchange for transferring his interest in K&M to Mace, Kelly received a \$40,000.00 promissory note from K&M, which note would become due if Mace sold K&M to a third party.⁷ Kelly also received

⁶The One-Year Agreement was admitted as Exhibit 1.

⁷The note, entitled Promissory Judgment Note, was admitted as Exhibit 4. The note states that its maturity date is May 1, 2008. There was no testimony or other evidence about why K&M - as opposed to Mace - gave the note in consideration of the transfer of stock to Mace by Kelly. It appears that Mace

the right to purchase K&M from Mace in exchange for \$40,000.00 and the release of Mace and Mace's real property from the business debt of K&M. Mace testified that the One-Year Agreement was intended to allow him to market K&M while Kelly attempted to secure financing to purchase K&M from Mace.

Skelton was neither a party to the One-Year Agreement nor involved in negotiating the One-Year Agreement. Rather, Mace stated that any agreement Skelton had to purchase K&M must have existed solely between Skelton and Kelly. Regarding Skelton and Kelly's possible agreement, Mace testified that "[Kelly] was the one going out to procure the loan and it was my understanding that [Skelton] was going to be part of that buy out."⁸ (Trial Tr. at 10:41:20.) Mace asserted that neither Skelton nor Kelly ever paid him the \$40,000.00 necessary for Kelly to purchase K&M.⁹

B. Skelton Testimony

Skelton, on the other hand, testified that an agreement existed among Mace, Kelly and himself, whereby Skelton was to become a "partner" in K&M. Skelton stated that he had four to six meetings with Mace and Kelly at the K&M Store in late 2001 and early 2002 regarding Skelton purchasing an interest in K&M. During the course

would be the beneficiary of any sale of K&M without taking any financial risk. Skelton did not sign the One-Year Agreement or the promissory note.

⁸A document entitled Stockholders Meeting, dated January 12, 2002, was admitted as Exhibit 2. Exhibit 2, which was signed by Mace, states, "Discussed buy out by Tim Kelly and Tom Skelton of Carl Mace stock that cannot happen because they cannot get funding." (Ex. 2 at 1.) Exhibit 2 indicates that only the Defendants were present at the meeting.

⁹Since Skelton was not a party to the One-Year Agreement or the promissory note, Skelton had no obligation to pay Mace \$40,000.00. (See note 7, *supra*.)

of these meetings, Skelton, Mace and Kelly reached an "understanding" or an "agreement" that Skelton would become a "partner" in or an "officer" of K&M in exchange for executing the Loan.¹⁰ (See *id.* at 10:57:19.) However, Skelton could not identify any particular event that signified when the oral agreement had been reached. Skelton testified that, as a "partner," he would receive stock in K&M, share in the profits and losses of K&M and participate in business decisions. Skelton did not know how much K&M stock he was to receive or from whom or when he would receive such stock, but Skelton assumed that he would receive a one-third ownership interest in K&M.¹¹ The agreement between Skelton, Mace and Kelly was never memorialized in writing.

Skelton testified that owning an interest in K&M would be beneficial to him as owner of the adjacent livestock auction because, for example, when he advertised an auction, information regarding sales on feed and other items could be included with the auction advertisement. Skelton was aware that Mace wished to be "bought out" of K&M, but Skelton wanted Mace to retain an interest in K&M due to Mace's financial and operational background. Skelton stated that he had no knowledge of the One-Year Agreement.

Prior to execution of the Loan, Skelton's accountant, Paul Thomas, reviewed financial statements of K&M, which Skelton believed

¹⁰"Loan" defined *infra* at page 9.

¹¹Skelton believed that he would receive his stock from "the stockholders," whom he mistakenly thought were Mace and Kelly. (See Trial Tr. at 11:22:53.)

were tax returns. Skelton understood that the assets of K&M included inventory and the K&M Store, although Skelton was aware that Jack Hanes had some interest in the K&M Store.¹² Skelton stated, "I wasn't sure whether [the K&M Store] was a rental or a purchase agreement at that point in time. . . . I was kind of left out in the dark about a couple of things." (*Id.* at 11:04:52.)

On May 24, 2002, Skelton and Kelly entered into a loan agreement with The First National Bank of Slippery Rock ("FNB") in the amount of \$347,000.00 to refinance K&M's existing debt with FNB ("Loan").¹³ As a consequence of the Loan, Mace's real property that served as collateral for K&M's existing debt was released. On that same date, in conjunction with the Loan, the Plaintiffs executed (i) Mortgage, which granted FNB a security interest in the Plaintiffs' farm located at 5186 South Raccoon Road, Canfield, Ohio ("Skelton Farm");¹⁴ and (ii) Guaranty, in which the Plaintiffs personally guaranteed repayment of the Loan¹⁵ (Loan, Mortgage and Guaranty, collectively, "Loan Documents").

Ultimately, Skelton never (i) received any interest in K&M; (ii) shared in the profits and losses of K&M; or (iii) participated

¹²Skelton testified that Jack Hanes previously operated a business at the location of the K&M Store.

¹³The Loan was admitted as Exhibit 6. Kelly signed the Loan as "president" of K&M and Skelton signed the Loan as "secretary/treasurer" of K&M. (Ex. 6 at 1.) Skelton testified that he was never an officer of K&M and did not know whether Kelly or FNB identified him as such in the Loan.

¹⁴The Mortgage was admitted as Exhibit A. The Mortgage contains a typographical error, which incorrectly states that the Skelton Farm is located in Pennsylvania, rather than Ohio. (See Ex. A at 2.)

¹⁵The Guaranty was admitted as page 14 of Exhibit A.

in any business decisions of K&M. After the Loan Documents were executed, Skelton met with K&M's corporate attorney to discuss the transfer of K&M stock to him. Skelton testified, "[E]vidently [the stock] had already been transferred to [Mace] and . . . [the corporate attorney] said I can't discuss that with you, because that's privileged information." (*Id.* at 11:06:00.) At "the end of 2003 or [2004]," Skelton contacted his accountant, Paul Thomas, who was also the accountant for K&M, to view the financial statements of K&M. Mr. Thomas told Skelton that K&M's financial statements were "private and confidential" and belonged to Mace. (*See id.* at 11:06:57.)

Skelton testified that, as early as 2004 or 2005, he sought to be released from the Loan as a guarantor and to have the Skelton Farm released as collateral.¹⁶ Mace repeatedly assured Skelton that Mace would attempt to refinance the Loan in order to have Skelton absolved of liability and to have the Skelton Farm released as collateral. On more than one occasion, Skelton accompanied Mace to FNB and Huntington Bank to attempt to refinance the Loan. However, the Loan was never refinanced and, on November 3, 2008, FNB filed a foreclosure action against the Skelton Farm in the Mahoning Court,

¹⁶Exhibit 13, which is a letter dated April 30, 2004, from Thomas D. Rodgers, Commercial Loan Officer for FNB, to Mace, states, "Tom Skelton called me last week and requested he be removed from the [L]oan as a guarantor, and asked if he could also have [the Skelton Farm] released as collateral for the [L]oan." (Ex. 13 at 1.)

which was denominated Case No. 2008 CV 4321 ("Foreclosure Action").¹⁷ On December 23, 2009, the Plaintiffs filed a third-party complaint against Mace in the Foreclosure Action.

III. DEFENDANT CINDY MACE

The Complaint does not make any reference to acts or statements by Defendant Cindy Mace. Rather, the Complaint addresses only actions of Carl Mace, individually and as president of K&M. Furthermore, neither the Stipulation nor the evidence presented at the Trial concerns Ms. Mace. Because the Plaintiffs failed to state any cause of action against or present any facts concerning Cindy Mace, the Court finds that she should be dismissed from this action.

IV. LAW & ANALYSIS

Section 523(a), which excepts various categories of debt from discharge, states, in pertinent part,

(a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt—

* * *

(2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by—

(A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition;

(B) use of a statement in writing—

¹⁷Exhibit C, Complaint for Foreclosure, states that First National Bank of Pennsylvania is the successor by merger to The First National Bank of Slippery Rock. As used in this opinion, "FNB" refers to both The First National Bank of Slippery Rock and First National Bank of Pennsylvania, successor by merger to The First National Bank of Slippery Rock.

(i) that is materially false;

(ii) respecting the debtor's or an insider's financial condition;

(iii) on which the creditor to whom the debtor is liable for such money, property, services, or credit reasonably relied; and

(iv) that the debtor caused to be made or published with intent to deceive; or

* * *

(4) for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny;

* * *

(6) for willful and malicious injury by the debtor to another entity or to the property of another entity[.]

11 U.S.C. § 523(a) (West 2012) (emphasis added). "The party moving for a finding of nondischargeability bears the burden to establish the applicable grounds by a preponderance of the evidence." *Reissig v. Gruber (In re Gruber)*, 436 B.R. 39, 41 (Bankr. N.D. Ohio 2010) (citing *Meyers v. I.R.S. (In re Meyers)*, 196 F.3d 622, 624 (6th Cir. 1999)).

Discharges in chapter 13 proceedings are governed by 11 U.S.C. § 1328. Section 1328 states, in pertinent part,

(a) Subject to subsection (d), as soon as practicable after completion by the debtor of all payments under the plan . . . the court shall grant the debtor a discharge of all debts provided for by the plan or disallowed under section 502 of this title, except any debt-

(1) provided for under section 1322(b)(5);

(2) of the kind specified in section 507(a)(8)(C) or in paragraph (1)(B), (1)(C), (2), (3), (4), (5), (8), or (9) of section 523(a);

* * *

(c) A discharge granted under subsection (b) of this section [hardship discharge] discharges the debtor from all unsecured debts provided for by the plan or disallowed under section 502 of this title, except any debt-

(1) provided for under section 1322(b)(5) of this title; or

(2) of a kind specified in section 523(a) of this title.

* * *

11 U.S.C. § 1328(a) and (c) (West 2012) (emphasis added).

"Unlike a discharge under section 727, a discharge under section 1328(a) discharges even those debts specified in 11 U.S.C. § 523(a)(6). See 11 U.S.C. § 1328(a). However, when a chapter 13 debtor moves for a so-called hardship discharge under 11 U.S.C. § 1328(b), all of the exceptions to discharge under section 523(a) apply. See 11 U.S.C. § 1328(c)(2)." *Fisher v. Fisher (In re Fisher)*, 2007 Bankr. LEXIS 1356, *11 (Bankr. N.D. Ohio Apr. 13, 2007) (emphasis added); see also *Holmes Lumber & Bldg. Ctr., Inc. v. Miller (In re Miller)*, 2010 Bankr. LEXIS 2760, *9 (Bankr. N.D. Ohio Sep. 2, 2010) (citations omitted) (unpublished) ("Section 523(a)(6) debts are covered by a general discharge in chapter 13 cases. Nondischargeability under 11 U.S.C. § 523(a)(6) only comes in to play in a chapter 13 case if a debtor seeks a hardship discharge under 11 U.S.C. § 1328(b)."); *Ambassadors Travel Servs., Inc. v. Liescheidt (In re Liescheidt)*, 404 B.R. 499, 504 (Bankr. C.D. Ill. 2009) ("[A] debtor who receives a full compliance

discharge is discharged from a Section 523(a)(6) debt, while one who receives the more limited hardship discharge is not.”)

A. Section 523(a)(2)(A)

To except a debt from discharge pursuant to § 523(a)(2)(A), the creditor must prove:

- (1) the debtor obtained money through a material misrepresentation that, at the time, the debtor knew was false or made with gross recklessness as to its truth;
- (2) the debtor intended to deceive the creditor;
- (3) the creditor justifiably relied on the false representation;
- and (4) its reliance was the proximate cause of loss.

Rembert v. AT&T Universal Card Servs., Inc. (In re Rembert), 141 F.3d 277, 280-81 (6th Cir. 1998) (citing *Longo v. McLaren (In re McLaren)*, 3 F.3d 958, 961 (6th Cir. 1993)). Actual fraud, as that term is used in § 523(a)(2)(A), “has been defined as intentional fraud, consisting in deception intentionally practiced to induce another to part with property or to surrender some legal right, and which accomplishes the end designed. It requires intent to deceive or defraud.” *Ash v. Hahn (In re Hahn)*, 2012 Bankr. LEXIS 651, **6-7 (Bankr. N.D. Ohio Feb. 6, 2012) (quoting *Mellon Bank, N.A. v. Vitanovich (In re Vitanovich)*, 259 B.R. 873, 877 (B.A.P. 6th Cir. 2001)).

At the Trial, the Plaintiffs argued that there were two incidents of fraud committed by Mace. First, the Plaintiffs asserted that Mace induced Skelton to execute the Loan Documents in exchange for an ownership interest in K&M, but that Mace never conveyed an interest in K&M to Skelton (“Count One”). (See Compl. ¶¶ 13-23.) Second, the Plaintiffs argued that Mace represented to

Skelton that he would obtain the release of the Plaintiffs and the Skelton Farm from the Loan, but that Mace failed to do so ("Count Two"). (See *id.* ¶¶ 24-31.)

1. Count One

"[Section] 523 requires as a threshold matter that there be a 'debt,' a term which is defined in the Bankruptcy Code." *Cirincione v. Cirincione (In re Cirincione)*, 2005 Bankr. LEXIS 831, *12 (Bankr. W.D. Mo. Apr. 12, 2005). "[I]t is the creditor who bears the burden of proving that a debt exists and that it is the type excepted from discharge under § 523." *Schloemer v. Moyer*, 2011 U.S. Dist. LEXIS 107367, *10 (S.D. Miss. Sep. 20, 2011) (citations and parentheticals omitted) (emphasis added). The Bankruptcy Code defines a "debt" as a "liability on a claim." 11 U.S.C. § 101(12) (West 2012). A "claim" is defined as a "right to payment." 11 U.S.C. § 101(5)(A). As stated by the Supreme Court, "[A] 'right to payment,' . . . 'is nothing more nor less than an enforceable obligation.'" *Cohen v. De La Cruz*, 523 U.S. 213, 218 (1998) (quoting *Penn. Dep't of Pub. Welfare v. Davenport*, 495 U.S. 552, 559 (1990)) (emphasis added).

As the basis for Count One, the Plaintiffs allege: (i) "[Mace] represented and warranted to Plaintiffs that Plaintiffs would receive a stock ownership in K&M, in return for execution of [the Loan Documents]" (Compl. ¶ 14); (ii) "Based on [Mace]'s representations and warranties, [Skelton] executed the [Loan] and Plaintiffs executed the [Guaranty] and Mortgage, as security for the [Loan]" (*id.* ¶ 15); and (iii) "Despite the representations and

warranties of [Mace], Plaintiffs were never provided stock in K&M, never received any of the income or profits from K&M, and never received any of the benefit from the [Loan] proceeds" (*id.* ¶ 21).

The parties stipulated that K&M was incorporated in Pennsylvania. More importantly, Skelton testified that the meetings among Mace, Kelly and himself, at which it was agreed that Skelton was to become a "partner" in K&M, took place at the K&M Store in Pennsylvania. Finally, the Mortgage was executed by the Plaintiffs in Butler County, Pennsylvania. (See Ex. A at 13.) It appears that the only nexus between the alleged fraud and the state of Ohio is that the Skelton Farm is located in Ohio. As a consequence, any claim for fraud that the Plaintiffs may have against Mace is governed by Pennsylvania law.

Mace argued that any claim based on fraud is barred by the applicable Pennsylvania statute of limitations. In Pennsylvania, the statute of limitations for claims of fraud is two years. See 42 Pa.C.S.A. § 5524(7) (West 2012).

"[T]he statute of limitations begins to run as soon as the right to institute and maintain a suit arises." *Fine v. Checcio*, 870 A.2d 850, 857 (Pa. 2005) (citing *Pocono Int'l Raceway, Inc. v. Pocono Produce, Inc.*, 468 A.2d 468, 471 (Pa. 1983)). "Mistake, misunderstanding, or lack of knowledge in themselves do not toll the running of the statute." *Id.* (citations omitted). An exception that tolls the statute of limitations is the discovery rule, which applies in instances "in which the injury or its cause was neither

known nor reasonably knowable." *Id.* at 858 (citations and parentheticals omitted). The discovery rule arises due to the "inability of the injured, despite the exercise of reasonable diligence, to know that he is injured and by what cause." *Id.* (citing *Pocono Int'l Raceway*, 468 A.2d at 471). "[R]easonable diligence is not an absolute standard, but is what is expected from a party who has been given reason to inform himself of the facts upon which his right to recovery is premised." *Id.*

Skelton's credible testimony establishes that Mace fraudulently induced Skelton to execute the Loan Documents in exchange for a promised ownership interest in K&M. The Court finds that the Plaintiffs incurred damages when Mace failed to transfer stock in K&M to Skelton. In closing argument, Mr. Chaney stated that the Plaintiffs were damaged by Mace's fraud, at the earliest, in May 2007 when K&M failed to satisfy the Loan upon its maturity. Mr. Chaney further suggested that the Plaintiffs did not incur damages until FNB declared the Loan to be in default on April 21, 2008.¹⁸ Despite Mr. Chaney's arguments to the contrary, the fact that K&M made payments on the Loan does not alter the nature of the Plaintiffs' damages, which arise from not receiving an ownership interest in K&M. The Plaintiffs' damages arise from this failure of consideration, not K&M's default on the Loan or the Foreclosure

¹⁸Mr. Chaney referenced Exhibit 20, which is a letter dated April 21, 2008, from Ronald R. Scarton, Vice President of Special Lending for FNB, to Mace. Exhibit 20 states, "Therefore, you are hereby advised that [FNB] considers this [L]oan to be in default and intends to pursue all rights and remedies to collect this debt." (Ex. 20 at 1.)

Action.

It is undisputed that (i) the Loan Documents were signed on May 24, 2002; and (ii) Skelton never received any interest in K&M. Because Mace's fraudulent representations were made prior to execution of the Loan Documents, as Skelton testified, the elements of fraud were satisfied and any cause of action related thereto accrued when Skelton did not receive an interest in K&M. Due to the discovery rule, the issue then becomes: when would a person exercising reasonable diligence have discovered that Skelton was damaged by Mace's misrepresentations?

According to Skelton, following execution of the Loan Documents, K&M's corporate attorney informed Skelton that any information regarding K&M was "privileged" and not available to him. In late 2003 or 2004, Paul Thomas, as accountant for K&M, told Skelton that K&M was owned by Mace and that Skelton could not view K&M's financial statements because they were "private and confidential." Finally, despite executing the Loan Documents in May 2002, Skelton never (i) received any evidence that he owned stock in K&M; (ii) shared in the profits or losses of K&M; or (iii) was consulted concerning any business decisions of K&M.

In light of Skelton's conversations with K&M's counsel and Paul Thomas, a person exercising reasonable diligence would have known, as of late 2003 or 2004, that Mace retained full control over K&M and Skelton had no ownership interest therein. Stated differently, a person exercising reasonable diligence would have recognized that

Skelton received nothing – and was not going to receive anything – in return for executing the Loan Documents. At the latest, Skelton had knowledge of his damages – *i.e.*, that he had not received an ownership interest in K&M – and that Mace’s fraud was the cause of such damages, by the end of 2004. The Court finds that the Plaintiffs’ cause of action for fraud in Count One is barred by the two-year statute of limitations in Pennsylvania.

Because Count One is barred by the statute of limitations for fraud, the Court finds that the Plaintiffs do not have an enforceable obligation based on fraud against Mace. The Bankruptcy Code defines a debt as a “liability on a claim.” 11 U.S.C. § 101(12) (West 2012). Accordingly, the Court finds that Mace does not owe a debt to the Plaintiffs based on fraud, as set forth in Count One. Since the Plaintiffs do not have an enforceable cause of action based on fraud, Count One fails to establish an exception to discharge for the Debt.

2. Count Two

In Count Two, the Plaintiffs allege: (i) “Subsequent to [FNB] defaulting K&M on the [L]oan . . . [Mace] . . . on several occasions represented and warranted to [Skelton] that [Mace] and/or K&M would obtain financing to satisfy the [Loan]” (Compl. ¶ 25); (ii) “Plaintiffs relied on [Mace]’s representations and warranties to their detriment, as evidenced by [FNB] seeking [the Foreclosure Action] on [the Skelton Farm]” (*id.* ¶ 29); and (iii) “Despite the representations and warranties of [Mace], [Mace] and K&M have failed

to obtain financing to satisfy the [Loan]" (*id.* ¶ 30). The Plaintiffs summarily conclude, "Based on the misrepresentation and fraud committed by [Mace], Plaintiffs are damaged." (*Id.* ¶ 31.)

Assuming, *arguendo*, that the allegations contained in Count Two are true, the Plaintiffs failed to establish the elements of fraud. To prevail on a § 523(a)(2)(A) claim based upon fraud, the Plaintiffs must establish: (i) Mace obtained money or property through a material misrepresentation that, at the time, Mace knew was false or made with gross recklessness as to its truth; (ii) Mace intended to deceive the Plaintiffs; (iii) the Plaintiffs justifiably relied on the false representation; and (iv) the Plaintiffs' reliance was the proximate cause of loss. See *Rembert v. AT&T Universal Card Servs., Inc. (In re Rembert)*, 141 F.3d 277, 280-81 (6th Cir. 1998). The Plaintiffs did not set forth any facts to indicate that Mace received any money or property in exchange for his promises to have the Plaintiffs and the Skelton Farm released from the Loan. Furthermore, there is no evidence that the Plaintiffs took any action whatsoever in reliance upon these representations and, as a result of such reliance, suffered damages. The Plaintiffs pledged the Skelton Farm as collateral for the Loan in 2002. Any damages arising from the Foreclosure Action involving the Skelton Farm arose from the pledge of collateral, not from the Foreclosure Action itself.

The evidence also indicates that Mace attempted (albeit unsuccessfully) to fulfill his promises to have the Plaintiffs and

the Skelton Farm released from the Loan. The parties stipulated that Mace unsuccessfully made the following attempts to have the Plaintiffs and the Skelton Farm released: (i) in March or April 2004, Mace requested the release of Skelton from the Loan; (ii) in April 2007, Mace offered his personal guarantee in exchange for the release of Skelton from the Loan; (iii) in April 2007, Mace offered to exchange a lien on the K&M Store¹⁹ in return for a release of the Skelton Farm; and (iv) Mace attempted to refinance the Loan with Huntington Bank in 2008 and offered FNB \$240,000.00 to settle the Loan in July 2008. In each instance, Mace's attempt was rebuffed by FNB or Huntington Bank. Mace's attempts to refinance the Loan indicate that he did not intend to deceive the Plaintiffs when he told Skelton that he would obtain refinancing to get the Plaintiffs and the Skelton Farm released from the Loan.

As set forth above, the Plaintiffs failed to establish that they relied on the representations serving as the basis for Count Two or suffered any damages as a result of such reliance. In addition, Mace did not receive any consideration in exchange for the representations that form the basis for Count Two. Moreover, the evidence does not show that Mace intended to deceive the Plaintiffs when he made those representations. As a consequence, the Court finds that the Plaintiffs failed to establish the elements of fraud with respect to Count Two. To the extent the Debt is based on

¹⁹Presumably, if Skelton had obtained the promised ownership interest in K&M, at the conclusion of the land contract, K&M – not Mace – would have owned the real estate. (See page 22 and note 20, *infra*.)

fraud, as set forth in Count Two, it is not excepted from discharge pursuant to § 523(a)(2)(A).

B. Section 523(a)(2)(B)

Section 523(a)(2)(B) excepts from discharge a debt for money or property obtained through the use of a materially false, written statement respecting the debtor's financial condition, so long as the debtor caused the statement to be made with intent to deceive and the creditor reasonably relied upon the statement. See 11 U.S.C. § 523(a)(2)(B) (West 2012). At the Trial, the Plaintiffs argued that Mace, as president of K&M, misrepresented the financial health of K&M through financial statements that inflated the value of K&M's assets. Specifically, the Plaintiffs asserted that K&M's financial statements falsely indicated that K&M owned the K&M Store, when, in fact, the K&M Store was owned by Jack Hanes. As Mace's testimony revealed, K&M entered into a land contract to purchase the K&M Store, which land contract was still in effect when the Loan Documents were executed. Mace further testified that the K&M Store was never owned by K&M but, instead, was transferred from Jack Hanes to Mace in 2006 or 2007 when the land installment contract had been fully performed.²⁰

The Plaintiffs' § 523(a)(2)(B) dischargeability claim fails for two reasons. First, Skelton testified that he did not rely on the misrepresentations contained in K&M's financial statements when he

²⁰There was no explanation about why the K&M Store was transferred to Mace when K&M – a separate corporate entity – had made the land contract payments.

executed the Loan Documents. Skelton testified he knew when he executed the Loan Documents that Jack Hanes may have owned a portion of the K&M Store or that K&M rented the K&M Store. Thus, the Plaintiffs' argument that the financial statements inflated the value of K&M by including the K&M Store as an asset is without consequence, since Skelton had actual knowledge that the K&M Store was not owned by K&M. Thus, the element of reasonable reliance is not present.

Second, there is no evidence that Mace caused the financial statements to be prepared with intent to deceive. Mace testified that, because he did not control the daily operations of K&M when the financial statements at issue were prepared - *i.e.*, the financial statements representing the assets and liabilities of K&M in 2001 and prior years - he had no input in the preparation of those financial statements. The Plaintiffs presented no evidence to rebut Mace's testimony that he was not involved in the preparation of the financial statements. As a consequence, the Court finds that the Plaintiffs failed to meet their burden of proof with respect to the elements of § 523(a)(2)(B).

C. Section 523(a)(4)

Section 523(a)(4) excepts from discharge any debt "for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny." 11 U.S.C. § 523(a)(4). Neither in the Complaint nor at the Trial did the Plaintiffs assert that a fiduciary relationship existed between the Plaintiffs and Mace or that Mace committed

embezzlement or larceny. Accordingly, the Court finds that the Debt is not excepted from discharge pursuant to § 523(a)(4).

D. Section 523(a)(6)

As stated *supra* at pages 11-14, debts for willful and malicious injury, as set forth in § 523(a)(6), are dischargeable pursuant to § 1328(a) if the debtor receives a full-compliance discharge upon completion of plan payments. See *Holmes Lumber & Bldg. Ctr., Inc. v. Miller (In re Miller)*, 2010 Bankr. LEXIS 2760, *9 (Bankr. N.D. Ohio Sep. 2, 2010) (citations omitted) (unpublished) (“Nondischargeability under 11 U.S.C. § 523(a)(6) only comes in to play in a chapter 13 case if a debtor seeks a hardship discharge under 11 U.S.C. § 1328(b).”) In the instant chapter 13 proceeding, the Defendants have not requested a hardship discharge pursuant to § 1328(b). In fact, the Defendants are not eligible to receive a hardship discharge because their Plan has not been confirmed. See 11 U.S.C. § 1328(b) (West 2012) (emphasis added) (“[A]t any time after the confirmation of the plan and after notice and a hearing, the court may grant a discharge to a debtor that has not completed payments under the plan only if-”); *Textron Fin. Corp. v. Hadley (In re Hadley)*, 2011 Bankr. LEXIS 3193, *39 (Bankr. E.D. Va. Aug. 19, 2011) (citing 11 U.S.C. § 1328(b)) (“In order for a court to grant a debtor a discharge per § 1328(b), the court must confirm the debtor’s Chapter 13 plan, hold a hearing, and find that each of the three elements in § 1328(b)’s subsections is present.”)

Because the Defendants are not presently eligible for a

hardship discharge, determination of whether the Debt is excepted from discharge pursuant to § 523(a)(6) is premature and not ripe for judgment. See *In re Miller*, 2010 Bankr. LEXIS 2760 at *10 ("As a result [of the debtor not having sought a hardship discharge], the court finds that the count under section 523(a)(6) is not ripe."); *Ambassadors Travel Servs. v. Liescheidt (In re Liescheidt)*, 404 B.R. 499, 504 (Bankr. C.D. Ill. 2009) ("Where a debtor is proceeding toward a full compliance discharge, that would by definition discharge a Section 523(a)(6) debt, there is no reason to litigate the issue of whether the debt is, in fact, one for a willful and malicious injury.") As a consequence, the Court will dismiss the Plaintiffs' § 523(a)(6) claim without prejudice to the Plaintiffs refiling a complaint if the Defendants request a hardship discharge or convert to a chapter 7 proceeding.

V. CONCLUSION

The Plaintiffs bear the burden to establish by a preponderance of the evidence that the Debt is non-dischargeable. The Plaintiffs presented no evidence concerning Defendant Cindy Mace. As a result, the Court will dismiss Cindy Mace as a defendant herein.

Skelton knew or should have known in late 2004, at the latest, that he had not and was not going to receive an ownership interest in K&M in exchange for the Plaintiffs' guarantee and pledge of the Skelton Farm for the Loan. As a consequence, the Plaintiffs' claim for fraud, as set forth in Count One, is barred by the two-year statute of limitations for fraud in Pennsylvania. Accordingly, the

Plaintiffs failed to meet their threshold burden, pursuant to § 523(a)(2)(A), to establish that Mace owes the Plaintiffs a debt based on fraud. Therefore, the Debt is not excepted from discharge pursuant to § 523(a)(2)(A). The Plaintiffs also failed to prove by a preponderance of the evidence that Mace prepared or caused to be prepared the financial statements reviewed by Skelton. Furthermore, Skelton had actual knowledge of the misstatements contained in K&M's financial statements and, thus, could not reasonably have relied on those misstatements. Accordingly, § 523(a)(2)(B) does not preclude discharge of the Debt.

The Plaintiffs did not present evidence sufficient to except the Debt from discharge pursuant to § 523(a)(4). Simply put, nothing in the record indicates that Mace acted in a fiduciary capacity or committed embezzlement or larceny.

Finally, § 523(a)(6) does not apply in a chapter 13 proceeding unless the debtor receives a hardship discharge pursuant to § 1328(b). Because the Defendants are not eligible for a hardship discharge at the present time and have not requested a hardship discharge, resolution of whether the Debt is excepted from discharge pursuant to § 523(a)(6) is not ripe for determination. Accordingly,

the Court will dismiss the Plaintiffs' claim pursuant to § 523(a)(6) without prejudice.

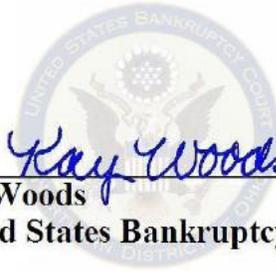
For the reasons set forth above, the Court will enter judgment in favor of the Defendants.

An appropriate order will follow.

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IT IS SO ORDERED.

Dated: May 7, 2012
04:58:27 PM



Kay Woods
 Kay Woods
 United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO

IN RE:

CARL V. MACE and
CINDY A. MACE,

Debtors.

* * * * *

THOMAS R. SKELTON and
AMY L. SKELTON,

Plaintiffs,

v.

CARL V. MACE and
CINDY A. MACE,

Defendants.

CASE NUMBER 10-42899

ADVERSARY NUMBER 10-4239

HONORABLE KAY WOODS

 ORDER FINDING THAT DEBT IS DISCHARGEABLE

This cause is before the Court on Complaint (Doc. # 1) filed by Plaintiffs Thomas R. Skelton and Amy L. Skelton a/k/a Amy Montgomery (collectively, "Plaintiffs") on November 1, 2010. The

Plaintiffs request the Court to find that the Debt owed to the Plaintiffs by Defendants/Debtors Carl V. Mace ("Mace") and Cindy A. Mace (collectively, "Defendants") is non-dischargeable pursuant to 11 U.S.C. § 523(a)(2), (a)(4) and (a)(6). On December 10, 2010, the Defendants filed Answer (Doc. # 6).

Trial was held in the instant adversary proceeding on February 29, 2012, at which appeared (i) John H. Chaney III, Esq. on behalf of the Plaintiffs; and (ii) Gary J. Rosati, Esq. on behalf of the Defendants.

For the reasons set forth in this Court's Trial Opinion Regarding Complaint to Determine Dischargeability of Debt entered on this date, the Court hereby:

1. Finds that the Plaintiffs failed to present any evidence concerning Defendant Cindy Mace;
2. Dismisses Defendant Cindy Mace from this proceeding;
3. Finds that the Plaintiffs failed to demonstrate by a preponderance of the evidence that the Debt is excepted from discharge pursuant to § 523(a)(2)(A);
4. Finds that the Plaintiffs failed to demonstrate by a preponderance of the evidence that the Debt is excepted from discharge pursuant to § 523(a)(2)(B);
5. Finds that the Plaintiffs failed to demonstrate by a preponderance of the evidence that the Debt is excepted from discharge pursuant to § 523(a)(4);
6. Finds that § 523(a)(6) does not apply in this chapter 13

proceeding;

7. Dismisses, without prejudice, the Plaintiffs' claim pursuant to § 523(a)(6); and
8. Enters judgment in favor of the Defendants.

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